

**STATE OF ILLINOIS**

**ILLINOIS COMMERCE COMMISSION**

Illinois Electric Transmission Company, LLC	:	
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Application for a Certificate of Public Convenience and Necessity, pursuant to Section 8-406 of the Public Utilities Act, to operate as a Public Utility, and for related approvals.	:	02-0742
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	:	(Cons.)
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Illinois Power Company	:	
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Petition for an Order (1) Concerning Classification of Illinois Power Company's Transmission and Distribution Facilities and (2) for Certain Determinations in Connection with the Sale of Illinois Power Company's Transmission System to Illinois Electric Transmission Company, LLC.	:	02-0743
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**PROPOSED INTERIM ORDER**

By the Commission:

**I. PROCEDURAL HISTORY**

On November 14, 2002, Illinois Electric Transmission Company, LLC ("IETC") filed a Petition for a Certificate of Public Convenience and Necessity ("IETC Petition"), pursuant to Section 8-406 of the Public Utilities Act ("Act"), to operate as a public utility, and for related approvals. This Petition is Docket No. 02-0742. Also on November 14, Illinois Power Company ("IP") filed a Petition ("IP Petition") for an order (1) approving the reclassification of its transmission and distribution facilities and (2) for certain determinations in connection with the sale of its transmission system to IETC. This Petition is Docket No. 02-0743. Separately, IP filed a Notice pursuant to Section 16-111(g) of the Act that IP is selling and transferring its transmission assets to IETC. This Notice was subsequently set for hearing and became Docket No. 02-0754. Docket Nos. 02-0742 and 02-0743 were consolidated, and, although it has not been consolidated with the other two, Docket No. 02-0754 is currently proceeding on a similar procedural schedule as the consolidated dockets.

In its Petition, IP specifically asks that its request for approval of the proposed reclassification of transmission and distribution facilities, which is Section II of IP's Petition, proceed on a schedule that would lead to an order on that portion of its Petition by on or

about January 14, 2003. IP filed prepared testimony and exhibits supporting the proposed reclassification with its Petition. IP also filed a motion requesting expedited consideration of the proposed reclassification. The present Interim Order only addresses Section II of IP's Petition.

Petitions to intervene were filed in Docket Nos. 02-0742 and 02-0743 by A.E. Staley Manufacturing Company, Archer-Daniels-Midland Company, Cargill, Inc., Caterpillar, Inc., Illinois Cement Company, Granite City Steel Division of National Steel Company, Olin Corporation, International Steel Group, Air Products & Chemicals Company, PPG Industries, Inc., and U.S. Silica Company as the Illinois Industrial Energy Consumers. The International Brotherhood of Electrical Workers, Local Union Nos. 51, 309, 702, and 1306 petitioned to intervene as well. Following the evidentiary hearing on this issue, Corn Belt Energy Corporation, Clinton County Electric Cooperative, Inc., Menard Electric Cooperative, Monroe County Electric Cooperative, Inc., Southwestern Electric Cooperative, Inc., Spoon River Electric Cooperative, Inc., Tri-County Electric Cooperative, Inc., and MJM Electric Cooperative, Inc. filed a joint petition to intervene. Commonwealth Edison Company also submitted a petition to intervene subsequent to the evidentiary hearing. Although some of the petitions to intervene are pending, all would-be interveners have been allowed to participate. Commission Staff ("Staff") participated as well.

At a pre-hearing conference on December 2, 2002, a separate schedule was adopted for the reclassification portion of IP's Petition. An evidentiary hearing was held on December 17, 2002 before a duly authorized Administrative Law Judge of the Commission at its offices in Springfield, Illinois. Appearances were entered by counsel for IP and by counsel for Staff. IP presented prepared testimony and exhibits of Paul D. Dare, IP's Director, Transmission Operations, and Michael T. Dryjanski, president of MTD Consulting and Services, Inc.<sup>1</sup> Staff presented the testimony of James D. Spencer, Senior Energy Engineer in the Engineering Department of the Energy Division of the Commission. At the conclusion of the hearing, the record concerning the proposed reclassification of IP's transmission and distribution facilities was marked "Heard and Taken." In light of Staff's agreement with IP's proposed reclassification, IP and Staff did not consider briefs necessary.

## **II. BACKGROUND TO THE PROPOSED RECLASSIFICATION**

These consolidated proceedings stem from IP and IETC entering into an agreement titled "Asset Purchase Agreement By and Among Illinois Electric Transmission Company,

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<sup>1</sup> Until late 2001, Mr. Dryjanski worked as an accountant at IP with primary responsibility for capital asset accounting.

LLC, Trans-Elect, Inc., Solely For Purposes of Article 5, Section 8.2 and Article 11, and Illinois Power Company Dated as of October 7, 2002" (the "APA") and related agreements that are exhibits to the APA, pursuant to which IP will sell to IETC, and IETC will thereafter own, operate, and maintain, the electric transmission system presently owned by IP. Under the APA, IP will sell to IETC those facilities that are classified as "transmission" under the "Seven-Factor Test" adopted by the Federal Energy Regulatory Commission ("FERC") in its Order No. 888.

In its 1999 Delivery Services Tariff ("DST") case, Docket Nos. 99-0120 and 99-0134 (Consolidated) ("1999 DST Case" or "1999 DST Order" as applicable), IP submitted an analysis classifying its transmission and distribution facilities, so that only the costs of its distribution facilities would be used in establishing its distribution services rate base. This analysis was conducted using the aforementioned Seven-Factor Test established FERC Order No. 888. In the 1999 DST Order, the Commission adopted the classification that was agreed to between IP and Staff. (See 1999 DST Order, Section III.C.2)

The Seven Factors set forth in FERC Order No. 888 are:

- (1) Local distribution facilities are normally in close proximity to retail customers.
- (2) Local distribution facilities are primarily radial in character.
- (3) Power flows into local distribution systems; it rarely, if ever, flows out.
- (4) When power enters a local distribution system, it is not reconsigned or transported on to some other market.
- (5) Power entering a local distribution system is consumed in a comparatively restricted geographical area.
- (6) Meters are based at the transmission/local distribution interface to measure flows into the local distribution system.
- (7) Local distribution systems will be of reduced voltage.

After the 1999 DST Order was issued, IP filed with FERC revisions to its transmission rates in its Open Access Transmission Tariff to reflect, *inter alia*, the classification of transmission and distribution facilities approved by this Commission in the 1999 DST Order. (See FERC Docket No. ER99-4415-000) On February 4, 2000, FERC issued an order in Docket Nos. ER99-3887-000, *et al.*, approving the classifications proposed by IP in Docket No. ER99-4415-000 (as well as those proposed by other Illinois utilities in separate FERC dockets). *MidAmerican Energy Co.*, 90 FERC & 61,105 (2000).

On October 12, 2000, FERC approved IP's offer of settlement for revised transmission rates, an offer which was premised on the classification of facilities that had previously been approved by both the Commission and FERC. *Illinois Power Co.*, 93 FERC & 61,036 (2000).

### **III. IP'S PROPOSED RECLASSIFICATION**

IP's Petition states that it conducted an analysis of its transmission and distribution facilities using the Seven-Factor Test and concluded that certain revisions were required to the previously approved classification. Exhibit 2 to IP's Petition, which has been entered into the evidentiary record as IP Exhibit 4.2, showed the proposed reclassification resulting from this analysis. The transmission assets that IP proposes to sell to IETC (as set forth in the Notice that is the subject of Docket No. 02-0754) are those assets classified as transmission facilities by the revised Seven-Factor Test analysis for which IP seeks approval in this Petition. IP will submit to FERC for its approval the revised classification as approved by this Commission. In order to permit FERC to rule on this aspect of the transaction in a timely fashion to support the proposed closing date of the asset transfer to IETC, IP requests that the Commission enter its order on the reclassification of assets by on or about January 14, 2003.

In support of its reclassification, IP offered the panel testimony of Messrs. Dare and Dryjanski. They presented the proposed reclassification of transmission and distribution facilities, including the original cost and original cost less depreciation of the facilities. They indicate that a reclassification is necessary for several reasons. First, three of the 69 kV lines that were classified as transmission in the 1999 DST Case should be classified as distribution, based on the FERC Seven Factors. Second, substations which were assigned to distribution by IP at the time of the reclassification presented in the 1999 DST Case were not evaluated at that time based on the Seven-Factor Test. An application of the Seven-Factor Test to these substations indicates that there are transmission facilities located within several of these substations. Third, further consideration of combination substations and transmission substations from the previous reclassification indicates that some revisions to the classifications of these substations are needed.

IP's witnesses indicate further that it is expected that IP or IETC (as IP's successor in ownership of the transmission system) will turn operational control of the transmission system currently owned by IP over to a regional transmission organization ("RTO") within the next few months. If the current classifications are continued after such transfer of operational control to the RTO, IP asserts that certain facilities which are distribution will remain improperly assigned to transmission and be placed under the control of the RTO as a transmission provider rather than under the control of IP as a local distribution company. Also, IP continues, certain facilities that are now classified as distribution are clearly essential to the operation of the transmission system and should be reclassified as

transmission. Upon transfer of operational control of the transmission system to a purchaser or an RTO, IP will become a transmission customer of the new owner or the RTO along with other wholesale customers connected to the transmission system. Without reclassification, IP states that an unacceptable situation would result in which it would continue to control facilities necessary to provide transmission services (other than wholesale distribution services) and would remain subject to the continued jurisdiction of FERC as a transmission provider.

With respect to electric lines, IP proposes that three 69 kV lines classified in the 1999 DST Case as transmission be reclassified to distribution. Those lines are Roseville Switching Station – Roseville (Central Illinois Public Services Company (“CIPS”)), Line 6630; Hillsboro Mine Spur, Line 6644A; and S. Woodson (CIPS) Interchange, Line 6654A. This reclassification was based on a review using the Seven-Factor Test. Following this review, IP’s witnesses conclude that these three lines should be reclassified as distribution. The IP witnesses applied the Seven Factors to these three 69 kV lines as follows: (1) Factor 1: these three lines are in close proximity to retail customers; (2) Factor 2: these three lines are primarily radial in character; (3) Factor 3: power flows on these lines into the local distribution system; (4) Factor 4: these lines are used to serve local load from alternate sources (they are not used to transport power from one utility to the other for any purpose other than the service of the local loads of the two concerned utilities); (5) Factor 5: power flowing on these lines is consumed in a comparatively restricted geographical area; (6) Factor 6: there are meters in place to measure the flows between the utilities; and (7) Factor 7: these three lines are 69 kV, which in all other cases IP has classified as distribution voltage.

In addition to the results of the Seven-Factor Test analysis, Messrs. Dare and Dryjanski explain that the classification of these lines as transmission had created a “transmission island” within IP’s distribution system, by which they mean that the lines in question are connected at either end to distribution facilities. This creates a situation in which transmission facilities are separated from the transmission system by the distribution system. IP states that this is contrary to the concept of an interconnected transmission system. Without contiguous transmission facilities connected to the transmission system, IP asserts that the power transported through these “transmission island” facilities can not be reconsigned or transported to other markets since it must pass through distribution facilities.

Finally, with respect to electric lines, Messrs. Dare and Dryjanski note that one 69 kV line that had been classified as transmission in the 1999 DST Case had in fact been sold to CIPS prior to 1999 and was therefore being removed from the facilities being classified. This line was Line 6618A (Savoy Tap).

With respect to substation facilities, Messrs. Dare and Dryjanski testify that the previous reclassification considered all substations with a secondary voltage below 69 kV as distribution substations. Two other substations were classified as distribution substations only because they are “customer substations.” These are substations that are typically installed for the purpose of service to a single retail customer. Application of the Seven-Factor Test to the substations with secondary voltages below 69 kV (which had not been considered in the previous classification) and the two “customer substations” revealed that several facilities in these substations functioned as transmission and failed many of the indicators of local distribution. The facilities in these substations which IP proposed to reclassify as transmission are not radial in character (failing Factor 2), have power flowing through the facilities rather than through them to the local distribution system (failing Factors 3 and 4), transmit power that often is reconsigned or transported through the facilities to other markets (failing Factor 4), transmit power much of which is not consumed in a restricted geographical area (failing Factor 5), lack metering to measure flows through the facilities (failing Factor 6) and do not operate at reduced voltages but at 138 kV which is typically transmission level voltage (failing Factor 7).

Similarly, IP’s witnesses explain that application of the seven factors to the substations which are currently classified as entirely transmission substations revealed some facilities in these substations are distribution because they function in a manner consistent with all of the seven indicators except for the absence of meters (Factor 6). Messrs. Dare and Dryjanski also indicate that IP proposes to reclassify the metering in substations which are currently classified as transmission substations to distribution plant when the metering is for the purpose of measuring energy going from the transmission system into the distribution system. This metering was not specifically considered in the previous classification. They also explained that, based on application of the Seven Factors, reclassification of some facilities was necessary due to changes in system configurations of existing facilities or addition of transformers, breakers, switches, or lines.

As a result of this review, Messrs. Dare and Dryjanski explain that no substations that were previously classified entirely as transmission were reclassified as entirely distribution. Likewise, no substations that were previously classified entirely as distribution have been reclassified as entirely transmission. IP reports, however, that this review resulted in more combination substations than in the original classification. Several of the substations that had been classified as entirely distribution have circuit breakers or switches which are properly classified as transmission based on the Seven Factors. These circuit breakers and switches, and equipment associated with the circuit breakers and switches, should be reclassified from distribution to transmission. Several of the substations that had been classified as entirely transmission have transformers, circuit breakers or switches which are properly classified as distribution based on the Seven Factors. These transformers, circuit breakers and switches and equipment associated with

these transformers, circuit breakers and switches should be reclassified from transmission to distribution.

Based on the proposed reclassification of facilities as described above, Messrs. Dare and Dryjanski then presented the results of the process employed by IP to functionalize the costs for the reclassified facilities. The process began with a review of the list of lines and substations that were reclassified. The list was then segregated into four categories: (1) transmission lines; (2) transmission-only substations; (3) combination substations that contain both distribution and transmission equipment; and (4) all other. The analysis of costs for each location in the lists of the transmission lines, transmission-only substations and combination substations was prepared based on data as of May 31, 2002 because at the time IP began its analysis, this was the most current information available. This information included assets that had been recorded in Account 101 (Utility Plant In Service), Account 106 (Completed Construction Not Classified), and Account 107 (Construction Work in Progress ("CWIP")).

For combination substations, IP's witnesses explain that the process was more involved. In combination substations certain assets in the substation perform a transmission function while others perform a distribution function, but the same asset does not perform both functions. For example, a breaker or a switch can be identified as providing a transmission function and not a distribution function. In order to properly segregate the costs between these two functions, it is necessary to isolate the cost of the asset and associate the cost with the function that it is serving. However, while it may be possible from an engineering perspective to associate an asset with either function, IP avers that there are a number of assets in its property records that could not easily be associated entirely with transmission or distribution. For bus and station conductor, a separate engineering estimate was prepared. This analysis identified by location a percentage of the asset cost that should be assigned to the transmission and distribution functions. For other assets such as cubicles, enclosures, outdoor supporting structures, wire and panels, if specific identification of the asset as transmission or distribution could not be made, IP states that the asset costs were categorized as common. A subsequent review was made of common asset groupings. IP indicates that the costs in each category were then reviewed and allocated based on a ratio of the count of major equipment items in the transmission and distribution categories. This ratio was developed by a count of the distribution breakers and transformers and the transmission breakers and transformers.

Also with respect to substations, Messrs. Dare and Dryjanski explain that certain assets such as land, fencing, buildings, and yard lighting serve both distribution and transmission functions. For the purposes of the cost analysis, assets such as these were classified as common assets. Based on the summation of the costs directly assigned to each function, a ratio of distribution and transmission costs was developed. This ratio was

then used to allocate the remaining costs from the common category to transmission and distribution for classification purposes.

According to IP's witnesses, the process described above is similar to the approach that IP used to assign and allocate common costs associated with those substations that were identified as combination in the 1999 DST Case.

Messrs. Dare and Dryjanski also testify how IP will record the common assets on its books and records. Based on the predominant use of the substation, i.e., transmission or distribution based on original cost, IP states that it will maintain the cost of common assets in the predominant category. For common assets retained by IP under the APA, the predominant category will be distribution in all cases. For Commission ratemaking purposes, IP will adjust its distribution rate base to account for costs that are supporting transmission. In accordance with the APA, if the predominant use of the substation is transmission, the common facilities will be transferred to the new owner.

IP's witnesses state further that if the predominant cost of the substation is distribution, ownership of the common assets will remain with IP. IP will then recover a portion of its revenue requirement associated with the common assets supporting the transmission function in accordance with the Distribution Transmission Interconnection Agreement ("DTIA") between IP and IETC, which is one of the agreements attached to the APA. Alternately, if the common assets have been sold to IETC because the substation is predominantly transmission, IP will be billed for costs in accordance with the DTIA for its *pro rata* share associated with the distribution facilities in the substation.

Messrs. Dare and Dryjanski also testify that for several reasons, the asset costs they presented in IP Exhibit 4.2, which, as noted above, were based on accounting data as of May 31, 2002, would not be the final amounts that IP will reclassify. They state that asset costs are dynamic in nature. Ongoing construction and retirement and replacement of assets will require an update of the costs as of the date of the sale of the transmission system to IETC. In addition, prior to December 31, 2002, IP and IETC will conduct joint reviews of the combination substations records (i.e., property records and engineering drawings) to confirm the assignments and review the allocations made in the reclassification analysis. They state that when necessary, a physical inspection of the facility will be made. They explain that these reviews may result in minor revisions to the allocations, but will not result in any change in the overall functional reclassification of the substation, and will be in strict accordance with the principles presented in their testimony. Messrs. Dare and Dryjanski also state that IP will file a final report with the Commission within six months following the date of sale showing the final classifications of facilities as transmission or distribution as of the date of the transmission system sale to IETC.

Although the final numbers are not yet available, IP's witnesses report that, based on



the cost data as of May 31, 2002 used in their analysis, the reclassification will result in the transfer of \$2.042 million of original cost from transmission to distribution and \$197,000 of CWIP from distribution to transmission. The related transfer of the accumulated provision for depreciation is \$2.461 million from transmission to distribution. This results in an increase of \$616,000 in the net book cost of transmission plant and a decrease of \$616,000 in the net book cost of distribution plant, based on cost data at May 31, 2002.

#### **IV. STAFF'S POSITION**

Staff witness Spencer testifies that he reviewed IP's filing with respect to its reclassification of facilities. He finds IP's proposed reclassification of the three 69 kV lines from transmission to distribution to be reasonable based on the Seven-Factor Test. He also agrees with the removal of the 69 kV line that had been sold to CIPS. In addition, Mr. Spencer finds no reason to oppose the proposed reclassification of substation facilities as described by IP in its testimony. He concludes that IP's application of the Seven-Factor Test to these facilities appears to be reasonable.

#### **V. COMMISSION CONCLUSION**

Based on its review of the record, the Commission concludes that IP's proposed reclassification of facilities between transmission and distribution, as presented on IP Exhibit 4.2, is reasonable and should be approved. IP's evidence supports and explains the proposed reclassification. Further, Staff found IP's reclassification based on the Seven-Factor Test to be reasonable, and found no reason to oppose the proposed reclassification.

No other party presented evidence concerning the proposed reclassification. However, as represented by Messrs. Dare and Dryjanski, IP should be required to file with the Commission, within six months following the closing of the sale of its transmission system to IETC, a report showing the final reclassification of facilities between transmission and distribution based on cost data as of the date of closing of the sale to IETC.

#### **VI. FINDINGS AND ORDERING PARAGRAPHS**

The Commission, having considered the entire record and being fully advised in the premises, is of the opinion and finds that:

- (1) IP is an Illinois corporation that is engaged in the transmission, distribution and sale of electric energy at retail in Illinois; IP is a "public utility" as that term is defined in Section 3-105 of the Act and an "electric utility" as that term is defined in Section 16-102 of the Act;
- (2) the Commission has jurisdiction over IP and the subject matter herein;

- (3) the determinations made and conclusions reached in the prefatory portion of this Interim Order are supported by the record, and are hereby adopted as findings of fact;
- (4) IP's proposed reclassification of facilities between transmission and distribution, as set forth on IP Exhibit 4.2, is reasonable and should be approved; and
- (5) IP should file a final report with the Commission within six months following the date of the sale of its transmission assets to IETC, showing the final classifications of facilities as transmission and distribution as of the date of the transmission system sale to IETC.

IT IS THEREFORE ORDERED that the reclassification of facilities between transmission and distribution submitted by Illinois Power Company is hereby approved.

IT IS FURTHER ORDERED that Illinois Power Company shall comply with Finding (5) of this Order.

IT IS FURTHER ORDERED that this Interim Order is not final and is not subject to the Administrative Review Law.

DATED: December 30, 2002.

Briefs on Exceptions must be received by January 3, 2003.

Briefs in Reply to Exceptions must be received by January 7, 2003.

Administrative Law Judge